

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF FARMDALE DEVELOPMENT) CASE NO. 2011-00048
CORPORATION FOR A RATE ADJUSTMENT)

ORDER

Pursuant to 807 KAR 5:076, Farmdale Development Corporation ("Farmdale Development") has applied for an adjustment of rates for sewer service. By this Order, the Commission establishes a rate that will produce additional annual revenues of \$21,393, an increase of 23.4 percent.

Farmdale Development, a Kentucky corporation, owns and operates sewage treatment facilities that serve approximately 234 customers in the Farmdale Subdivision of Franklin County, Kentucky.

On February 9, 2011, Farmdale Development filed its application with the Commission for an adjustment of its monthly rate from \$32.60 to \$42.38, an increase of 30 percent.¹ On July 6, 2011, Commission Staff issued a report of its findings and recommendations regarding the proposed rate and Farmdale Development's operations during the test period. It found that, based upon Farmdale Development's test-period operations, Farmdale Development required total revenues of \$108,266 to meet its reasonable operating expenses and earn a reasonable rate of return. It further found that, to reach this level of revenue, Farmdale Development required a rate adjustment

¹ On March 23, 2011, Farmdale Development filed with the Commission a revised tariff that contained its proposed rate and stated an effective date of April 28, 2011. On April 15, 2011, the Commission suspended the proposed rate for five months.

to generate additional annual revenue of \$16,815, or 18.38 percent, over normalized revenue from rates of \$91,541. Commission Staff recommended that Farmdale Development be authorized a monthly rate of \$38.56.

Considering the recommended rates to be inadequate, Farmdale Development filed objections to Commission Staff's findings and recommendations and requested a hearing in this matter. After extended discussions, Farmdale Development and Commission Staff entered into a stipulation regarding the principal issues in this matter.² They filed the Stipulation with the Commission on August 8, 2011. Farmdale Development withdrew its request for a hearing and moved for a decision based upon the existing record.

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. The calendar year ending December 31, 2009 should be used as the test period to determine the reasonableness of Farmdale Development's existing and proposed rates.
2. Based upon pro forma test-period operations, Farmdale Development's pro forma annual revenues are \$91,451.
3. Based upon pro forma test-period operations, Farmdale Development's pro forma total operating expenses, after adjusting for known and measurable changes, is \$92,558. The Appendix to this Order provides a breakdown of Farmdale Development's pro forma operating expenses.

² No person has sought or been granted intervention in this proceeding.

4. Farmdale Development has Interest on Long-term Debt or Other Interest Expense of \$7,665.

5. Farmdale Development's pro forma Amortization expense of \$8,967 includes rate case expenses of \$4,362 for legal expenses (\$2,362) and rate consultant fees (\$2,000) that Farmdale Development incurred to pursue its rate adjustment application. These expenses are amortized over a three-year period.

6. Combined pro forma Owner/Manager Fee expense and Maintenance of Treatment & Disposal expense is \$10,611.

7. Farmdale Development's pro forma insurance expense is \$543.

8. Given that no basis exists to determine an appropriate rate of return for Farmdale Development, the use of an operating ratio³ to determine its total revenue requirement is appropriate.⁴

9. An operating ratio of 0.88 will permit Farmdale Development to meet its reasonable operating expenses and provide a fair and reasonable return for equity growth and should be used to determine Farmdale Development's total revenue requirements.

10. Applying an operating ratio of 0.88 to Farmdale Development's pro forma total operating expenses of \$92,558 produces a revenue requirement without interest

³ Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

⁴ See, e.g., Case No. 8468, *An Adjustment of the Rates of Plantation Hill Sewage Treatment Plant, Inc.* (Ky. PSC Jun. 25, 1982); 1 A.J.G. Priest, *Principles of Public Utility Regulation* (Michie 1969) 220-224.

expense of \$105,179. When interest expense is considered, Farmdale Development has a total revenue requirement of \$112,844, or \$21,393 in additional annual revenue than Farmdale Development's current rate produces.

11. Given Farmdale Development's end of test-period customer level of 234 customers and considering the effects of rounding, a monthly rate of \$40.19 will produce the required total revenue requirement.

12. A monthly rate of \$40.19 is a fair, just, and reasonable rate for the services that Farmdale Development currently provides to its customers.

13. Farmdale Development's proposed rate will produce revenues in excess of those found reasonable herein and should be denied.

14. The Commission's decision with regard to the level of Owner/Manager Fee should not be misinterpreted. This Order does not establish a standard rule to be uniformly applied to small utilities for ratemaking purposes. To the contrary, rate recovery of payments to utility owner/managers should be determined on a case-by-case basis. The Commission's decisions will vary according to the circumstances of the utility's operations.

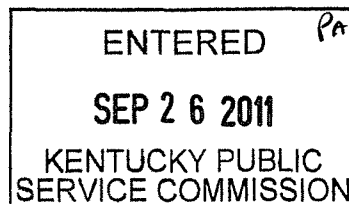
15. Applicants seeking recovery of an Owner/Manager Fee through rates must provide substantial evidence of the services that the owner/manager provides and the time required to provide such services. This evidence must be provided each time that an application for rate adjustment is filed. Reliance upon past Commission decisions without accompanying evidence will be insufficient to meet the applicant's burden of proof.

16. Applicants seeking recovery of rate case expenses through rates must provide substantial evidence that these expenses are reasonably incurred. To the extent that less costly alternatives are available to permit an applicant to pursue its application, an applicant will be expected to demonstrate that its use of a more costly alternative is reasonable and is not to the detriment of ratepayers.

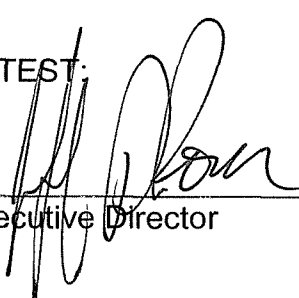
IT IS THEREFORE ORDERED that:

1. Farmdale Development's motion that this matter be decided upon the existing record is granted.
2. Farmdale Development's proposed rate for sewer service is denied.
3. Farmdale Development is authorized to assess a monthly fee of \$40.19 for sewer service provided on and after the date of this Order.

By the Commission



ATTEST:



Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
 COMMISSION IN CASE NO. 2011-00048 DATED **SEP 26 2011**

Owner/Manager Fee/ Maintenance of Treat. & Disp.	\$10,611
Sludge Hauling	2,650
Utility Service-Water	2,202
Other Labor, Materials	8,570
Fuel & Power Expense	17,508
Chemicals	1,840
Routine Maintenance Fee	13,020
Maintenance of Collection System	1,565
Agency Collection Fee	9,154
Maintenance of Other Plant	98
Office Supplies and Other	844
Outside Services Employed	9,504
Regulatory Commission Expense	250
Insurance Expense	543
Rent	600
Depreciation Expense	1,747
Amortization Expense	8,967
Taxes Other Than Income	2,885
Total Operating Expenses	\$92,558

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